

Financial Statements

**West Michigan Community
Mental Health System**

September 30, 2004



Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name West Michigan Community Mental Health System	County Mason
Audit Date 9/30/04	Opinion Date 11/17/04	Date Accountant Report Submitted to State: 3/22/05	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☒ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ Yes ☒ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ Yes ☐ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☒ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☒ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ Yes ☒ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☒ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☒ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☒ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	✓		
Reports on individual federal financial assistance programs (program audits).			✓
Single Audit Reports (ASLGU).			✓

Certified Public Accountant (Firm Name) Roslund, Prestage & Company, P.C.			
Street Address 308 Gratiot Avenue		City Alma	State MI
Accountant Signature <i>Roslund, Prestage & Company, P.C.</i>		ZIP 48801	Date 3/22/05

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INDEPENDENT AUDITOR'S REPORT

West Michigan Community Mental Health System
Ludington, Michigan

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of West Michigan Community Mental Health System (the Authority), as of and for the year ended September 30, 2004, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amount and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Authority as of September 30, 2004, and the respective changes in financial position and cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 17, 2004 on our consideration of the Authority's internal control over financial reporting and our test of its compliance with certain provisions of laws, regulations, contracts and grants. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis on pages I-V, and budgetary comparison information on pages 29-30, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming opinions on the financial statements that collectively comprise the Authority's basic financial statements. The other supplemental information listed in the table of contents is presented for purposes of additional analysis and are not a required part of the basic financial statements of the Authority. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Roslund, Prestage & Company, P.C.

Roslund, Prestage & Company, P.C.
Certified Public Accountants

November 17, 2004

**MANAGEMENT DISCUSSION
AND ANALYSIS**

**West Michigan Community Mental Health System
Financial Statements for the Fiscal Year Ended September 30, 2004
Management's Discussion and Analysis**

The management of West Michigan Community Mental Health System (WMCMHS) presents the following discussion and analysis of the financial activities during the fiscal year 2003/2004. This discussion and analysis is provided to introduce the basic financial statements of the past year and to provide the reader information to help assess whether the financial position has improved or deteriorated as a result of the year's operation. Please read this section in conjunction with the auditor's report, our financial statements, notes to the financial statements, and supplemental information taken as a whole to get a comprehensive understanding of WMCMHS' financial position.

Fiscal year 2002/2003 began a new funding mechanism for WMCMHS. Under the new contractual requirements issued by the Michigan Department of Community Health (MDCH), WMCMHS no longer received its Medicaid funding directly from the state. Instead, Medicaid funding for mental health service began to be paid to regional Pre-paid Inpatient Health Plan (PIHP). WMCMHS, under an affiliation agreement with Northern Lakes Community Mental Health Authority (formally North Central and Great Lakes Community Mental Health Authorities) became a member of the Northwest Community Mental Health Affiliation serving a nine county region. The significance of this funding arrangement and the impact on the provision of services to the residents of Lake, Mason and Oceana Counties has little noticeable impact on our service delivery system. WMCMHS continues to receive 36.11% of our revenue directly from MDCH and other sources for non-Medicaid services provided to Lake, Mason, and Oceana county residents.

Basic Financial Statement

Two types of financial statement are provided: **Government – wide Statements** and **Fund Statements**.

Government – wide financial statements are designed to present the organization's finances in a layout similar to that of a private sector business. They consist of a Statement of Net Assets (providing historical balance sheet information), which shows the difference between assets and liabilities; and a Statement of Activities (providing historical income statement information), which shows revenues and expenses and the change in net assets from the previous year. Information presented in these statements is on the full accrual basis of accounting.

West Michigan Community Mental Health System
Financial Statements for the Fiscal Year Ended September 30, 2004
Management's Discussion and Analysis

Fund financial statements report information using the modified accrual basis of accounting. They offer a series of statements that focus on the major governmental funds. For WMCMHS, the major funds consist of the general fund and the proprietary fund. The general fund statements identify activities of our day-to-day operations. The proprietary fund identifies funds set aside in our Internal Service Fund for risk management. Reconciliations are also offered between the Fund Financial Statements and the Government-wide Statements.

Comparison with Prior Year

West Michigan CMH System's total net assets show an increase for fiscal year 2003/2004 as compared to the prior year, restated in a comparative format, from \$5,819,306 to \$5,981,275. Total assets decreased by 4.0 percent and total liabilities decreased by 19.3 percent. Unreserved net assets changed from \$2,593,727 to \$2,808,037. This is an increase of \$214,310 to those funds able to finance general operations without restrictions.

Net Assets

	Governmental Activities	
	2004	2003
Current and Other Assets	7,563,929	7,814,689
Capital Assets	496,398	581,994
Total Assets	8,060,327	8,396,683
Current Liabilities	1,496,953	2,180,457
Non-Current Liabilities	582,099	396,920
Total Liabilities	2,079,052	2,577,377
Net Assets:		
Invested in capital assets, net of debt	496,398	581,994
Restricted	2,676,840	2,643,585
Unrestricted (deficit)	2,808,037	2,593,727
Total Net Assets	5,981,275	5,819,306

West Michigan Community Mental Health System
Financial Statements for the Fiscal Year Ended September 30, 2004
Management's Discussion and Analysis

Analysis of Overall Financial Position

WMCMHS continues to improve our financial standing with an increase of \$426,245 to net assets. DCH revenues increased 5.7% with the implementation of the Adult Benefit Waiver program. Medicaid revenue was virtually unchanged from FY 03 when the adjustment for the reinvestment plan is considered. WMCMHS's expenditures were reduced from the prior year by \$71,964, which includes the purchase of real property. The table below illustrates net asset activity compared with last fiscal year.

Changes in Net Assets

	Governmental Activities	
	2004	2003
Revenues		
DCH	3,802,884	3,599,329
Medicaid	8,872,254	8,172,229
Grant, Contracts & Other Revenues	671,365	794,567
Local	539,196	579,080
Total Revenues	13,885,699	13,145,205
Expense		
Personnel	7,275,772	7,326,227
Capital Outlay	150,000	18,493
Other Expenses	6,031,552	6,185,698
Debt Payments - Principal	633	
Debt Payments - Interest	1,497	
Total Expense	13,459,454	13,530,418
Revenue Over/(Under) Expense	426,245	(385,213)
Adjusted for Prior years Reinvestment Plan	-	660,802
Increase (decrease) in Net Assets	426,245	275,589

**West Michigan Community Mental Health System
Financial Statements for the Fiscal Year Ended September 30, 2004
Management's Discussion and Analysis**

Capital Assets and Long-Term Debt

Capital Assets increased by \$150,000 with the purchase of real property in Scottville, Michigan. The property had previously been leased by WMCMHS and run by a third party as a staffed group home. WMCMHS will continue to contract with the third party for operation of the home. A ten-year balloon loan was entered into for the purchase of the property at an interest rate of 5.8%. The building will be depreciated over a 20-year useful life and reflected as a capital asset on the Statement of Net Assets. Monthly depreciation and interest expense will total less than previous monthly lease payments, resulting in an overall positive effect on WMCMHS future financial position.

Medicaid Reinvestment and General Fund Carryforward

West Michigan CMH System was able to establish the five percent maximum allowable general fund carryforward. The Northwest Community Mental Health Affiliation experienced a Medicaid reduction of \$2.2 million. Even under these circumstances, the affiliation was able to establish a Medicaid Reinvestment savings of approximately one and one-half percent based on contributions of its' affiliate members due to effective control of expenditures.

Analysis of Significant Budget Variations

Amendments to fiscal year 2003/2004 budget show no significant changes to total expenditures, with an original budget of \$13,376,537 and a final budget reduced to \$13,266,864. The amendment consisted of several line item variations. The most significant change was shifting dollars from salary to professional contracts for locum tenens used during a staffing shortage. Recruitment efforts were successful and the new Psychiatrist was hired in September. Other changes included transferring budgeted contingency to offset variable cost overruns. The revenue budget had no noteworthy change as the overall modification was less than 1% of original budget, and was spread amongst various funding sources.

**West Michigan Community Mental Health System
Financial Statements for the Fiscal Year Ended September 30, 2004
Management's Discussion and Analysis**

Currently Known Information Effecting the Future

The State of Michigan continues to be faced with a budget shortfall. The State's financial difficulties are compounded by high unemployment rates and federal deficits reflecting the weak economic condition throughout the country. These factors all present potential future funding issues for community mental health and specialty supports and services, which makes the near term outlook very uncertain. Revenues from the State are expected to be flat at best with no inflationary adjustments, while increases in service demands are expected in part as a result of economic factors. Another funding element of note is the State has undertaken the process to re-base the rates for Medicaid capitation payments. The rate changes are to be effective for the next fiscal year (starting October, 2005). Depending on when this information is released, Pre-paid Inpatient Health Plans and their affiliates may need to address Medicaid funding reductions. While the financial position of the Authority is currently healthy, the economic outlook will continue to put significant pressure on our ability to serve and support our consumers. Should significant reductions occur in our funding, WMCMHS management will analyze the services delivered, looking at alternatives where appropriate, to determine where costs may be reduced or where revenues may be enhanced.

**GOVERNMENT-WIDE
FINANCIAL STATEMENTS**

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF NET ASSETS
SEPTEMBER 30, 2004 AND 2003

	Governmental Activities	
	2004	2003
Assets		
Current Assets		
Cash and Cash Equivalents - Unrestricted	\$5,087,280	\$5,349,329
Due from Other Governmental Units	141,063	214,917
Prepaid Expenses	176,513	159,970
Total Current Assets	5,404,856	5,724,216
Noncurrent Assets		
Restricted Investments	2,159,073	2,090,473
Capital Assets - Depreciable, Net	496,398	581,994
Total Noncurrent Assets	2,655,471	2,672,467
Total Assets	8,060,327	8,396,683
Liabilities		
Current Liabilities		
Accounts Payable	537,740	739,513
Deferred Revenue	169,098	589,017
Due to Other Governmental Units	144,448	246,231
Accrued Liabilities	6,805	6,675
Retirement Payable	39,429	32,885
Post-Employment Benefits Payable	9,139	12,638
Accrued Wages and Other Payroll Liabilities	586,190	553,498
Current Portion of Notes Payable	4,104	-
Noncurrent Liabilities		
Notes Payable	145,263	-
Compensated Absences	436,836	396,920
Total Liabilities	2,079,052	2,577,377
Net Assets		
Invested in Capital Assets	496,398	581,994
Reserved for Risk Management	929,759	919,156
Reserved for Future Capital Outlay	1,747,081	1,724,429
Unreserved and Undesignated	2,808,037	2,593,727
Total Net Assets	\$5,981,275	\$5,819,306

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2004 AND 2003

Functions	<u>Expenses</u>	<u>Program Revenues</u>		<u>Net (Expense) Revenue and Changes Net Assets</u>	<u>2003</u>
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>		
Governmental Activities					
Health & Welfare - Mental Health	<u>\$13,551,759</u>	<u>\$9,014,050</u>	<u>\$4,616,675</u>	\$78,966	(\$772,381)
General Revenues					
Unrestricted Investment Earnings				72,400	100,963
Restricted Investment Earnings				<u>10,603</u>	<u>16,362</u>
Total General Revenues and Contributions				<u>83,003</u>	<u>117,325</u>
Change in Net Assets				161,969	(655,056)
Net Assets - October 1				<u>5,819,306</u>	<u>6,474,362</u>
Net Assets - September 30				<u>\$5,981,275</u>	<u>\$5,819,306</u>

The notes to the financial statements are an integral part of this statement.

FUND FINANCIAL STATEMENTS

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
BALANCE SHEET
GOVERNMENTAL FUNDS
SEPTEMBER 30, 2004 AND 2003

	General Fund	
	2004	2003
Assets		
Cash and Cash Equivalents - Unrestricted	\$5,087,280	\$5,349,329
Cash and Cash Equivalents - Restricted	2,159,073	2,090,473
Due from Other Governmental Units	141,063	214,917
Prepaid Expenses	176,513	159,970
Total Assets	\$7,563,929	\$7,814,689
Liabilities		
Accounts Payable	\$537,740	\$739,513
Deferred Revenue	169,098	589,017
Due to Other Governmental Units	144,448	246,231
Due to Other Funds	929,759	919,156
Accrued Liabilities	6,805	6,675
Retirement Payable	39,429	32,885
Post-Employment Benefits Payable	9,139	12,638
Accrued Wages and Other Payroll Liabilities	586,190	553,498
Total Liabilities	2,422,608	3,099,613
Fund Balance		
Reserved for Prepaid Expenses	176,513	159,970
Reserved for Future Capital Outlay	1,747,081	1,724,429
Unreserved and Undesignated	3,217,727	2,830,677
Total Fund Balance	5,141,321	4,715,076
Total Liabilities and Fund Balance	\$7,563,929	\$7,814,689

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
RECONCILIATION OF FUND BALANCES ON THE BALANCE SHEET FOR GOVERNMENTAL FUNDS
TO NET ASSETS OF GOVERNMENTAL ACTIVITIES ON THE STATEMENT OF NET ASSETS
FOR THE YEAR ENDED SEPTEMBER 30, 2004

Total fund balance - governmental funds	\$5,141,321
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	
Add: capital assets	1,471,388
Deduct: accumulated depreciation	(974,990)
An internal service fund is used by management to cover the risk of overspending the Managed Care Specialty Services Program contract. The assets and liabilities of the internal service fund are included in governmental activities in the statement of net assets.	
Add: net assets of governmental activities accounted for in the internal service fund	929,759
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported as liabilities in the funds. Long-term liabilities at year end consist of:	
Deduct: Loans payable	(149,367)
Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:	
Deduct: compensated absences	<u>(436,836)</u>
Net assets of governmental activities	<u><u>\$5,981,275</u></u>

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2004 AND 2003

Revenues	General Fund	
	2004	2003
State Grants		
Department of Community Health Contract	\$3,435,748	\$3,586,900
Adult Benefit Waiver	355,527	-
MI Child	11,609	12,429
Title XX	4,047	4,047
Tobacco Tax	-	4,350
RICC	2,022	1,643
TBRA	47,012	11,968
Respite Block Grant	4,599	-
Total State Grants	<u>3,860,564</u>	<u>3,621,337</u>
Federal Grants		
Wraparound Grant	70,873	323,315
Strong Families / Safe Children	37,100	38,395
Transportation Grant	47,143	43,870
PAS / ARR Grant	104,100	146,889
Total Federal Grants	<u>259,216</u>	<u>552,469</u>
Contributions - Local Units		
County Appropriations	<u>325,000</u>	<u>325,000</u>
Charges for Services		
Medicaid - Subcontract with North Central CMH	8,357,291	8,091,275
Medicaid - Other	514,963	80,954
Client and Third Party Pay	141,796	153,117
Total Charges for Services	<u>9,014,050</u>	<u>8,325,346</u>
Interest and Rents		
Interest	<u>72,400</u>	<u>100,963</u>
Other Revenue		
Proceeds from Sale of Assets	34,066	19,692
Proceeds from Loan	150,000	-
MRS Supported Employment	-	13,440
ISD Grant	-	24,852
Sheltered Workshop	36,694	70,712
Mason / Lake ISD	46,094	56,550
Miscellaneous	87,615	34,844
Total Other Revenue	<u>354,469</u>	<u>220,090</u>
Total Revenues	13,885,699	13,145,205

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2004 AND 2003

Expenditures	General Fund	
	2004	2003
Health & Welfare - Mental Health		
Personnel Costs	\$7,275,772	\$7,326,227
Operating Expenditures	6,031,552	6,185,698
Capital Outlay	150,000	18,493
Debt Payments - Principal	633	-
Debt Payments - Interest	1,497	-
Total Expenditures	<u>13,459,454</u>	<u>13,530,418</u>
Revenues Over (Under) Expenditures	426,245	(385,213)
Fund Balance, October 1	4,715,076	4,762,109
Prior Period Adjustment	-	338,180
Fund Balance, September 30	<u>\$5,141,321</u>	<u>\$4,715,076</u>

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2004

Net change in fund balances - total governmental funds	\$426,245
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures and the proceeds from loans to finance capital purchases as revenue. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense and the loan proceeds are recorded as a liability.	
Add: capital outlay	150,000
Deduct: depreciation expense	(203,022)
Deduct: loan proceeds	(150,000)
Payment of principal on long-term debt is an expenditure in the governmental funds, but it reduces long-term liabilities in the statement of net assets and does not affect the statement of activities.	
Add: Principal paid on notes payable	633
Sales proceeds from the disposal of capital assets are recorded as revenue in the governmental funds. However, in the statement of activities they are netted against the basis in the disposed capital assets resulting in a gain or loss.	
Deduct: Proceeds from disposal of capital assets	(32,036)
Deduct: Loss on disposal of capital assets	(538)
An internal service fund is used by management to cover the risk of overspending the Managed Care Specialty Services Program contract. The net revenue (expense) of the fund attributable to those funds is reported with governmental activities.	
Add: interest income from governmental internal service fund	10,603
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the funds.	
Less: increase in accrual for compensated absences	(39,916)
Change in net assets of governmental activities	<u>\$161,969</u>

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
SEPTEMBER 30, 2004 AND 2003

		Internal Service Funds	
		2004	2003
Assets			
	Due from Other Funds	<u>\$929,759</u>	<u>\$919,156</u>
Net Assets			
	Restricted	<u>\$929,759</u>	<u>\$919,156</u>

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2004 AND 2003

	Internal Service Funds	
	2004	2003
Non-Operating Revenues (Expense)		
Interest Income	\$10,603	\$16,362
Change In Net Assets	10,603	16,362
Net Assets, Beginning of Year	919,156	902,794
Net Assets, End of Year	<u>\$929,759</u>	<u>\$919,156</u>

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED SEPTEMBER 30, 2004 AND 2003

	Internal Service Fund	
	2004	2003
Cash Flows from Operating Activities		
Adjustments to Reconcile Net Income		
to Net Cash Provided by Operating Activities:		
(Increase) Decrease In:		
Due from Other Funds	(\$10,603)	(\$16,362)
Net Cash Provided (Used) From Operating Activities	(10,603)	(16,362)
Cash Flows from Investing Activities		
Interest Income	10,603	16,362
Net Change in Cash and Cash Equivalents	-	-
Cash and Cash Equivalents, Beginning Of Year	-	-
Cash and Cash Equivalents, End Of Year	-	-
Reconciliation of Operating Income To Net Cash Provided		
By (Used for) Operating Activities:		
Operating Income (Loss)	NA	NA

The notes to the financial statements are an integral part of this statement.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of West Michigan Community Mental Health System (the Authority) conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the significant accounting policies used by the Authority.

In June of 1999, the GASB issued Statement No. 34, Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments. Significant changes in the Statement include the following:

- A Management’s Discussion and Analysis (MD&A) section providing an analysis of the Authority’s overall financial position and results of operations.
- Financial statements prepared using full accrual accounting for all of the Authority’s activities.
- A change in the fund financial statements to focus on major funds.

These and other changes are reflected in the accompanying financial statements (including the notes to the financial statements). The Authority has implemented the provisions of Statement No. 34 effective October 1, 2002.

A. Reporting Entity

West Michigan Community Mental Health System is a separate legal public entity established by an interlocal agreement between Lake, Oceana, and Mason Counties pursuant to the Urban Cooperation Act. The West Michigan Community Mental Health System elected to become a Mental Health Authority effective January 1, 1998 under the provisions of Act 258 – Public Acts of 1974, as amended. The purpose of the Authority is to provide a range of mental health services for persons located within the three counties. The Authority’s operations are largely funded by grants from federal, state and local funds.

The accompanying financial statements have been prepared in accordance with criteria established by the Governmental Accounting Standards Board for determining the various governmental organizations to be included in the reporting entity. These criteria include significant operational financial relationships that determine which of the governmental organizations are a part of the Authority’s reporting entity, and which organizations are legally separate, component units of the Authority. Based on the application of the criteria, the Authority does not contain any component units.

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all of the activities of the Authority. *Governmental activities* normally are supported by intergovernmental revenues.

The statement of activities demonstrates the degree to which the direct expenses of a function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges to consumers who purchase, use or directly benefit from services provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues.

Net assets are restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally it is the Authority's policy to use restricted resources first, then unrestricted resources as they are needed.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements.

C. Measurement Focus, Basis of Accounting and Basis of Presentation

Government-Wide Financial Statements – The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental Fund Financial Statements - The Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Authority considers revenues to be available if they are collected within 60 days of the end of the current fiscal year end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

West Michigan Community Mental Health System
Notes To Financial Statements

An exception to the "60 day" rule is the recognition of certain patient fee revenues and the related receivables. The Authority has elected to recognize these revenues on the cash basis of accounting, which is in compliance with the Department of Community Health's revenue recognition formula. The difference between the cash basis of accounting and modified accrual basis of accounting for these revenues are not material to the financial statements.

Modifications to the accrual basis of accounting include:

- Employees' vested annual leave is recorded as expenditures when utilized. The amount of accumulated annual leave unpaid at September 30, 2004, has been reported only in the government-wide financial statements.
- Interest on general long-term obligations is recognized when paid.
- Debt service expenditures and claims and judgments are recorded only when payment is due.

Proprietary Fund Financial Statements – The financial statements of the proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The principal operating revenues of the internal service fund are charges to other funds for insurance services. Operating expenses for internal service funds include the cost of claims, administration and reinsurance. Any revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The financial activities of the Authority that are reported in the accompanying financial statements have been classified into the following major governmental and proprietary funds.

Governmental Funds

General Fund – This fund is the Authority's primary operating fund. It accounts for all financial resources of the Authority, except those required to be accounted for in other funds.

West Michigan Community Mental Health System
Notes To Financial Statements

Proprietary Funds

Internal Service Fund - This fund represents amounts set aside to fund the net uninsured exposure of potential shortfalls of contract revenues.

D. Budgetary Data

Budgets are adopted by the Authority for all governmental funds. The budget is adopted and prepared on the modified accrual basis of accounting. The budget is also adopted at the function level. The budgeted revenues and expenditures for governmental fund types, as presented in this report, include any authorized amendments to the original budget as adopted.

E. Cash and Cash Equivalents

The Authority's cash and cash equivalents are considered to be cash on hand, money market funds, demand deposits and short-term investments with an original maturity of three months or less from the date of acquisition. Investments are stated at cost.

Michigan Compiled Laws, Section 129.91, authorized the Authority to deposit and invest in the accounts of Federally insured banks, credit unions, and savings and loan associations; bonds, securities and other direct obligations of the United States, or any agency or instrumentality of the United States; United States government or Federal agency obligation repurchase agreements; bankers' acceptance of United States banks; commercial paper rated by two standard rating agencies within the two highest classifications, which mature not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions which are rated investment grade; and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan. Financial institutions eligible for deposit of public funds must maintain an office in Michigan. The Authority's deposits are in accordance with statutory authority.

F. Receivables and Payables between Funds

Activity between funds that are representative of lending / borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to / from other funds" (i.e. the current portion of interfund loans) or "advances to / from other funds" (i.e. the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due / to other funds". Any residual balances outstanding between the governmental activities are reported in the government-wide financial statements as "internal balances".

West Michigan Community Mental Health System
Notes To Financial Statements

G. Receivables

Accounts receivable in all funds report amounts that have arisen in the ordinary course of business and are stated net of allowances for uncollectible amounts.

Due from other governmental entities consist primarily of amounts due from the Michigan Department of Community Health and the State of Michigan.

H. Prepaid Items

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

I. Inventories

The Authority does not recognize as an asset inventories of supplies. The cost of these supplies is considered immaterial to the financial statements and the quantities are not prone to wide fluctuation from year to year. The costs of such supplies are recorded as an expenditure when purchased.

J. Capital Assets

Capital assets, which include buildings, equipment and furnishings, computers and software, and vehicles, are reported in the governmental column in the government-wide financial statements. Capital assets are defined by the government as individual assets with an initial cost equal to or more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during construction of capital assets is not capitalized. No interest expense was incurred during the current year.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements.

A salvage value equal to 15% of the original cost has been established for all vehicles.

West Michigan Community Mental Health System
Notes To Financial Statements

Capital assets of the Authority are depreciated using the straight line method over the following estimated useful lives:

Assets	Years
Buildings	20
Equipment and Furnishings	5 – 20
Computers and Software	3 – 5
Vehicles	4

K. Restricted Investments

The Authority has charged to the Department of Community Health the vested portion of compensated absences as of September 30th. The Authority holds, in a separate bank account, funds equal to or greater than the compensated absences liability. The use of these funds is restricted to payment of compensated absences as they come due.

The Authority has also charged to the Department of Community Health an amount designated for future improvements and/or acquisition of major capital assets. The Authority holds, in a separate bank account, funds equal to the amount charged to the Department and the use of these funds is restricted to improvements and/or acquisitions as indicated in the plan established and approved by the Authority.

L. Governmental Fund – Fund Balance Reserves and Designations

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditure or (2) legally segregated for a specific future use. The reserves for related assets such as prepaid items are examples of the former. Reserves for Medicaid Savings, compensated absences and post-employment benefits are examples of the latter.

M. Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

N. Inpatient / Residential Cost Liability

The amount recorded for inpatient/residential liability is based on management's estimate. This estimate is based on 1) the number of clients at each facility, 2) the number of days each client is at each facility, and 3) the daily rate charged for each facility.

The Authority does not receive actual billings for these services until several months after the service date. Therefore, the liability is not liquidated within the normal 60-day period after year-end. Also, the actual cost may vary from the estimated due to reimbursements from third party payers that are applied to the total cost before the billings are sent to the Authority.

O. Deferred Revenue

Deferred revenues arise when the Authority receives resources before it has a legal claim to them. In subsequent periods, when the revenue recognition criterion is met, or when the Authority has a legal claim to the resources, the liability for deferred revenue is removed from the fund financial statements and government-wide financial statements, and revenue is recognized.

P. Grants

Grants from the Department of Community Health (DCH) and other governmental units are recorded as revenues when the actual expenditures financed by the grant are incurred. Excess funding is treated as deferred until used or until retrieved by the source.

Q. Comparative Data

Comparative total data for the prior year has been presented in the accompanying financial statements in order to provide an understanding of changes in the Authority's financial position and operations. Also, certain amounts presented in the prior year data have been reclassified in order to be consistent with the current year's presentation.

NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Information

Annual budgets are adopted at the function level and on a basis consistent with generally accepted accounting principles for all governmental funds. All annual appropriations lapse at fiscal year end. The Authority does not maintain a formalized encumbrance accounting system.

West Michigan Community Mental Health System
Notes To Financial Statements

B. Excess Of Expenditures Over Appropriations

P.A. 621 of 1978, Section 18(1), as amended, provides that a local unit shall not incur expenditures in excess of the amount appropriated. Budgets for the budgetary funds were adopted at the functional level and have been presented at the functional level in this report. During the year ended September 30, 2004 and 2003, The Authority incurred expenditures in excess of the amounts budgeted as shown on the budget comparison schedule in the back of this report.

NOTE 3 - DETAIL NOTES

A. Cash And Investments

Cash

At year-end, the carrying amount of the Authority's cash and cash equivalents was as follows:

Cash & Cash Equivalents	2004	2003
Petty Cash	\$565	\$760
Checking, Savings, And Money Market Accounts	492,232	796,187
Certificates of Deposit	3,541,621	2,009,705
Certificates of Deposit – Restricted	1,747,081	1,724,429
Commercial Paper	1,052,862	2,542,677
Municipal Investment Fund – Restricted	411,992	366,044
Totals	\$7,246,353	\$7,439,802

The bank balance at year end was \$7,561,582 of which \$400,000 was covered by federal depository insurance and \$7,161,582 was uninsured and uncollateralized. Some of the deposits that exceed FDIC insurance coverage are held at local banks.

The Authority believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, the Authority evaluates each financial institution with which it deposits government funds and accesses the level of risk of each institution. Only those institutions with an acceptable estimated risk level are used as depositories.

The municipal investment fund in the amount of \$411,992 is restricted to payment of compensated absences as they come due. The certificate of deposit in the amount of \$1,747,081 is restricted for future improvements and/or acquisition of major capital assets.

The carrying amount shown above approximates their fair value.

West Michigan Community Mental Health System
Notes To Financial Statements

Investments

In accordance with GASB Statement 3, investments are classified into three categories of credit risk as follows:

- Category 1: Insured or collateralized with securities held by the Authority or its agent in the Authority's name.
- Category 2: Collateralized with securities held by the pledging financial institution's trust department or agent in the Authority's name.
- Category 3: Uncollateralized (includes any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent, but not in the Authority's name).

Investment	Category 3	Carrying Amount	Market Value
Commercial Paper	\$1,052,862	\$1,052,862	\$1,052,862

B. Interfund Receivables And Payables

The amounts of the interfund receivables and payables at September 30, 2004 are as follows:

Fund	Due From	Due To
General Fund	-	\$929,759
Internal Service	\$929,759	-

C. Due From Other Governmental Units

Due from other governmental units as of September 30th consists of the following:

Due From	2004	2003
State of Michigan – Medicaid	\$56,172	\$59,535
State of Michigan – OBRA	5,616	42,014
State of Michigan – Transportation Grant	17,045	12,651
State of Michigan – FIA	5,915	19,323
State of Michigan – Wraparound	32,745	27,382
State of Michigan – Tenant Based Housing Assist. Grant	6,805	9,008
State of Michigan – DCH Cost Settlement	-	25,425
State of Michigan – Respite	2,460	-
MRS	-	13,440
Mason & Lake ISD	3,471	6,139
County Appropriations	10,834	-
Totals	\$141,063	\$214,917

West Michigan Community Mental Health System
Notes To Financial Statements

D. Prepaid Expenses

Prepaid expenses represent payments for the following expenses that will benefit future periods:

Prepaid	2004	2003
Insurance	\$161,524	\$145,094
Dues	6,656	6,543
Rent	8,333	8,333
Totals	\$176,513	\$159,970

E. Capital Assets

A summary of changes in capital assets is as follows:

Governmental Activities	Beginning Balance	Increases	Decreases	Ending Balance
Buildings	-	\$150,000	-	\$150,000
Equipment and Furnishings	\$387,294	-	-	387,294
Computers and Software	305,194	-	-	305,194
Vehicles	762,175	-	(\$133,275)	628,900
Sub-total	1,454,663	150,000	(133,275)	1,471,388
Accumulated Depreciation	(872,669)	(203,022)	100,701	(974,990)
Totals	\$581,994	(\$53,022)	(\$32,574)	\$496,398

F. Deferred Revenue

Deferred revenue represents amounts received in advance of the period in which they were earned as follows:

Deferred Revenue	2004	2003
5% Carryforward – DCH	\$168,598	\$175,044
Medicaid Savings	-	413,973
Other	500	-
Totals	\$169,098	\$589,017

West Michigan Community Mental Health System
Notes To Financial Statements

G. Due To Other Governmental Units

Due to other governmental units as of September 30th consist of the following:

Due To	2004	2003
State of Michigan – Inpatient/Residential	\$42,796	\$42,016
State of Michigan – Medicaid	-	72,004
State of Michigan – DCH Risk Authorization	-	11,516
Due to PHP	23,092	-
Community Inpatient & Crisis Residential	78,560	120,695
Totals	\$144,448	\$246,231

H. Accrued Liabilities

This liability represents state and federal income taxes and other amounts withheld from paychecks prior to year end but not remitted until after year end.

I. Accrued Wages and Other Payroll Liabilities

This liability represents amounts paid to employees during October that was earned during September. Also included are employer payroll taxes and related liabilities.

J. Retirement Liability

This liability represents amounts due to the retirement system based on wages earned as of September 30th of each year.

K. Post-Employment Benefits Payable

Prior to the existence of the WMCMHS, the County of Mason provided health insurance for employees of Mason County (including employees of the Mental Health Authority) who retired at age sixty with ten years of service with the County until they reach the age of sixty-five. After the age of sixty-five, retired employees with ten years of service with the County shall have their Medicare supplement paid by the County. When the WMCMHS was created, the employees of the Mason County Mental Health Board became employees of WMCMHS. Therefore, the Authority was required to assume the responsibility to pay the health insurance premiums for the Mason County retirees as stated under the original agreement between the County of Mason and its employees. Therefore, the amount recorded as Post-Employment Benefits Payable represents the estimated liability for these health insurance premiums.

The balance in this liability at September 30, 2004 and 2003 is \$9,139 and \$12,638, respectively.

West Michigan Community Mental Health System
Notes To Financial Statements

L. Long-Term Debt

COMPENSATED ABSENCES

The WMCMHS's policy allows employee's to accumulate paid time off pay and to carry this accumulation into the future. The paid time off pay that was earned but not yet paid as of September 30, 2004 and 2003 was \$436,836 and \$396,920, respectively.

MORTGAGE PAYABLE

On July 13, 2004 the Authority borrowed \$150,000 to finance the purchase of a building. The terms of the loan calls for 119 monthly payments of \$1,065 and a final payment of \$97,459 on July 13, 2014. The interest rate is stated at 5.8%.

The changes in the long-term debt are as follows:

Description of Debt	Beg. Bal. 10/01/03	Additions	Reductions	End. Bal. 9/30/04
Mortgage Payable	\$-0-	\$150,000	\$633	\$149,367

The annual payment of principle and interest for the next five years is as follows:

Year Ended September 30 th ,	Principle and Interest Due
2005	\$12,777
2006	12,777
2007	12,777
2008	12,777
2009	12,777
2010 – 2014	154,955

M. Fund Balance Reserves and Designations

A portion of the fund balance at September 30th has been reserved equal to the amount of prepaid expenses, since prepaid expenses do not constitute "available spendable resources."

A portion of fund balance (\$1,747,081) has been designated by the Authority to be used for future improvements and/or acquisition of major capital assets.

Net assets have been reserved in the amount of \$929,759 for the expected future risk corridor requirements of the MCSSP contract. See additional note below.

West Michigan Community Mental Health System
Notes To Financial Statements

N. Operating Leases

West Michigan Community Mental Health System has entered into various operating leases for the use of real and personal property. Operating leases do not give rise to property rights or lease obligations, and therefore, the results of the lease agreements are not reflected in the financial statements.

The following is a schedule of the future minimum lease payments required under the operating leases that have initial or remaining noncancelable lease terms as of September 30, 2004:

Year Ending September 30th	Amount
2005	\$177,682
2006	176,265
2007	154,564
2008	116,146
2009	100,000
Thereafter	400,000

4. OTHER INFORMATION

A. Compliance Audits

All governmental grants are subject to a transactional and compliance audit by the grantors or their representatives. Therefore, an indeterminable contingency exists for expenditures, which may be disallowed by the granting agencies.

B. Pension Plan

The Authority is in an agent multiple-employer defined benefit pension plan with the Municipal Employees' Retirement System (MERS) administered by the State of Michigan. The system provides for the following provisions: normal retirement, deferred retirement, service retirement allowance, disability retirement allowance, non-duty death allowance, duty death allowance, and post-retirement adjustments to plan members and their beneficiaries. The most recent period for which actuarial data was available was for the year ending December 31, 2003.

MERS was organized pursuant to Section 12a of Act #156, Public Acts of 1851 (MSA 5.333(a); MCLA 46.12(a)), as amended, State of Michigan. MERS is regulated under Act No. 427 of the Public Acts of 1984, sections of which have been approved by the State Pension Commission. MERS issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to the MERS at 447 North Canal Street, Lansing, Michigan 48917-9755.

West Michigan Community Mental Health System
Notes To Financial Statements

During the fiscal year ended September 30, 2004, the Authority's contributions made in accordance with contribution requirements determined by an actuarial valuation was zero. The billings by the MERS were based on the 2003 valuation. The employer contribution rate has been determined based on the entry age normal funding method. Under this method, the total actuarially-determined contribution requirement is the sum of the normal cost and the payment required to amortize the unfunded accrued liability over the amortization period of 30 years, less the accelerated funding credit, if available.

The normal cost is the cost of benefit rights accruing on the basis of current service. Significant actuarial assumptions used include a long-term investment yield rate of 8 percent and annual salary increases of 4.5% based on an age-related scale to reflect merit, longevity, and promotional salary increases.

The following table presents information required by GASB Statements Number 25 and 27.

GASB 25 INFORMATION	
Actuarial Accrued Liability:	
Retirees and Beneficiaries Currently Receiving Benefits	\$2,285,980
Terminated Employees Not Yet Receiving Benefits	271,612
Current Employees – Accumulated Employee Contributions Including Allocated Investment Income Employer Financed	114,248 1,132,115
Total Actuarial Accrued Liability	3,832,779
Net Assets Available For Benefits At Actuarial Value (market value \$4,013,112)	4,395,004
Unfunded (Overfunded) Actuarial Accrued Liability	(\$562,225)
GASB 27 INFORMATION	
Fiscal Year Beginning	Oct. 1, 2005
Annual Required Contributions (ARC)	\$20,472
Amortization Factor Used – Underfunded Liabilities (33 years)	.051679
Amortization Factor Used – Underfunded Liabilities (25 years)	.058519
Amortization Factor Used – Overfunded Liabilities (10 years)	.119963

Additional information regarding the pension plan of West Michigan Community Mental Health System can be found in the annual Report issued by Gabriel, Roeder, Smith and Company.

The Authority entered into an administrative service agreement between The International City Management Association Retirement Corporation ("ICMA") and MERS on December 22, 1998. MERS has entered into an Alliance Agreement with ICMA providing for ICMA to serve as plan administrator for the defined contribution plans of municipalities participating in MERS.

West Michigan Community Mental Health System
Notes To Financial Statements

The ICMA Retirement Trust (the "Trust") is a common law trust governed by an elected Board of Trustees for the commingled investments of retirement funds held by state and local governmental units for their employees. The ICMA acts as investment advisor to the Trust and has designed, and offers, a series of separate funds for the investment of plan assets.

Employer contributions to the Trust for the year ended September 30, 2004 and 2003 were \$497,503 and \$500,679, respectively.

Additional information can be obtained by writing to: Executive Director, West Michigan Community Mental Health System, 920 Diana Street, Ludington, Michigan, 49431.

C. Money Purchase Pension Plan

The Authority has established a pension plan to provide funds for the employee's retirement. The plan is known as the West Michigan Mental Health System Money Purchase Pension Plan and became effective on January 1, 1996 and was amended effective January 1, 1997. This plan is a "qualified" plan, as defined in section 401(a) of the Internal Revenue Code of 1986, as amended. It also qualifies as a "governmental plan", as defined in section 414(d) of the Code.

The plan is funded exclusively through the purchase of annuity contracts from the Variable Annuity Life Insurance Company (VALIC). If permitted by the Employer, annuities from other companies may be offered.

All employees can be eligible to receive Employer contributions (including nonelective contributions) under the Plan except the following: employees covered by social security, board of directors, on-call employees, leased employees, and individuals not on the payroll who are classified as independent contractors. There are no age or service requirements. Eligible employees will be eligible for Employer contributions upon the date that employment begins.

The Authority will make contributions to the Plan equal to 5 percent of compensation (not in excess of the Social Security Taxable Wage Base). The contributions to the plan for the year ended September 30, 2004 and 2003 were \$258,071 and \$264,141, respectively.

Additional information about the plan can be obtained by writing to: Executive Director, West Michigan Community Mental Health System, 920 Diana Street, Ludington, Michigan, 49431.

D. Risk Management

The Authority is exposed to various risks of loss related to theft of, damage to, and destruction of assets; errors and omissions; injuries; and natural disasters. The Authority participated in the public entity risk pool – Michigan Municipal Risk Management Authority (MMRMA) for auto and general liability, property and crime and vehicle physical damage coverage.

MMRMA, a separate legal entity, is a self-insured association organized under the laws of the State of Michigan to provide self-insurance protection against loss and risk management services to various Michigan governmental entities.

As a member of this pool, the Authority is responsible for paying all losses, including damages, loss adjustment expenses and defense cost, or each occurrence that falls within the member's self-insured retention. If a covered loss exceeds the Authority's limits, all further payments for such loss are the sole obligation of the Authority. If for any reason the Authority's resources available to pay losses are depleted, the payment of all unpaid losses of the Authority is the sole obligation of the Authority.

The Authority's coverage limits include \$15,000,000 for liability, \$1,500,000 for vehicle physical damage, and \$3,515,121 for buildings and personal property. The annual premium paid for the period of January 1, 2003 to January 1, 2004 was \$125,708.

Also, the Authority authorized the establishment of an Internal Service Fund to account for funds to be used to cover the risk of overspending their authorized projected revenues covered by the Managed Care Specialty Services Program (MCSSP) contract.

The MCSSP contract entered into by the Authority provides for the use of Department of Community Health funding for the establishment of an Internal Service Fund that is restricted for use only to meet the expected future risk corridor requirements of the MCSSP contract. Expenditures from the Internal Service Fund will occur when, in any one fiscal year, the Authority finds it necessary to expend more to provide services necessary to carry out the MCSSP contract requirements than revenue provided to the Authority by the contract.

E. Prior Period Adjustments

Prior period adjustments shown in the fund level financial statements in this report represent the adjustment to fund balance due to the following:

Adjustment	2003
Removal of compensated absences liability at 10/1/02	\$349,121
Adjustments to cost settlement for fiscal year ended 9/30/02	(10,941)
Total Increase (Decrease) To Fund Balance	\$338,180

West Michigan Community Mental Health System
Notes To Financial Statements

F. Compliance Audit

In June 2001 the Michigan Office of Auditor General issued their report on their performance audit of West Michigan Community Mental Health System (WMCMHS). The audit included an examination of WMCMHS's records and activities for the period October 1, 1998 through September 30, 2000.

In August 2002 The Department of Community Health issued their report on their performance audit of West Michigan Community Mental Health System (WMCMHS). The audit included an examination of WMCMHS's records and activities for the same period - October 1, 1998 through September 30, 2000.

As a result of these audits numerous issues have emerged and are currently progressing through various stages of dispute resolution, administrative appeal, and judicial review.

The Department of Community Health is requesting \$3,368,121 from WMCMHS.

The resolutions of these audit issues could have a material impact on the financial statements of WMCMHS.

These financial statements do not reflect any contingent liabilities relating to these audit findings or the amounts requested.

As of the date of this report this issue has not been resolved.

A complete copy of that report is available by writing to:

West Michigan Community Mental Health System
920 Diana Street
Ludington, Michigan 49431

West Michigan Community Mental Health System
Notes To Financial Statements

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REQUIRED SUPPLEMENTAL INFORMATION

BUDGETARY COMPARISON SCHEDULE

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - BUDGET AND ACTUAL
GENERAL FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2004

	Budgeted Amounts		Actual	Variances Between Actual and Final Budget
	Original	Final		
Revenues				
State Grants	\$3,759,216	\$3,819,105	\$3,860,564	\$41,459
Federal Grants				
Wraparound Grant	60,000	60,000	70,873	10,873
Strong Families / Safe Children	38,395	41,757	37,100	(4,657)
Transportation Grant	47,143	47,143	47,143	-
PAS / ARR Grant	135,572	135,572	104,100	(31,472)
Total Federal Grants	281,110	284,472	259,216	(25,256)
Contributions - Local Units				
County Appropriations	325,000	325,000	325,000	-
Charges for Services				
Medicaid - DCH Contract	8,489,825	8,489,825	8,357,291	(132,534)
Medicaid - Other	70,000	70,000	514,963	444,963
Client and Third Party Pay	142,040	117,194	141,796	24,602
Total Charges for Services	8,701,865	8,677,019	9,014,050	337,031
Interest and Rents				
Interest	85,434	48,326	72,400	24,074
Other Revenue				
Proceeds from Sale of Assets	45,000	38,135	34,066	(4,069)
Proceeds from Loan	-	-	150,000	150,000
Sheltered Workshop	61,164	29,424	36,694	7,270
Mason / Lake ISD	55,315	55,315	46,094	(9,221)
Miscellaneous	65,862	15,447	87,615	72,168
Total Other Revenue	227,341	138,321	354,469	216,148
Total Revenues	13,379,966	13,292,243	13,885,699	593,456

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - BUDGET AND ACTUAL
GENERAL FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2004

	Budgeted Amounts			Variances Between Actual and Final Budget
	Original	Final	Actual	
Expenditures				
Health & Welfare - Mental Health				
Current:				
Personnel Costs	\$7,510,896	\$7,244,959	\$7,275,772	(\$30,813)
Operating Expenditures	5,825,641	6,008,905	6,031,552	(22,647)
Capital Outlay	40,000	13,000	150,000	(137,000)
Debt Payments - Principal	-	-	633	(633)
Debt Payments - Interest	-	-	1,497	(1,497)
Total Expenditures	<u>13,376,537</u>	<u>13,266,864</u>	<u>13,459,454</u>	<u>(192,590)</u>
Revenues Over (Under) Expenditures	3,429	25,379	426,245	400,866
Fund Balance, October 1	<u>4,715,076</u>	<u>4,715,076</u>	<u>4,715,076</u>	<u>-</u>
Fund Balance, September 30	<u>\$4,718,505</u>	<u>\$4,740,455</u>	<u>\$5,141,321</u>	<u>\$400,866</u>

The notes to the financial statements are an integral part of this statement.

OTHER SUPPLEMENTAL INFORMATION

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF PERSONNEL EXPENDITURES
FOR THE YEAR ENDING SEPTEMBER 30, 2004 AND 2003

Governmental Fund Types

	<u>General Fund</u>	
	<u>2004</u>	<u>2003</u>
Personnel Costs		
Salaries And Wages	\$5,277,355	\$5,418,285
Fringe Benefits	<u>1,998,417</u>	<u>1,907,942</u>
Total Personnel Costs	<u><u>\$7,275,772</u></u>	<u><u>\$7,326,227</u></u>

The notes to the financial statements are an integral part of this statement.

WEST MICHIGAN COMMUNITY MENTAL HEALTH SYSTEM
STATEMENT OF OPERATING EXPENDITURES
FOR THE YEAR ENDING SEPTEMBER 30, 2004 AND 2003

Governmental Fund Types

	General Fund	
	2004	2003
Operating Expenditures		
Supplies	\$135,506	\$157,784
Building Rent	210,309	226,751
Utilities	148,465	157,770
Repairs and Maintenance	195,727	224,323
Insurance	201,623	153,450
Marketing / Membership	52,665	44,940
Professional Contracts	504,937	468,430
Contractual Services	3,386,434	3,229,162
Other Contractual	104,769	318,250
Board Expenses	8,987	9,949
Consumer Panel	3,375	2,846
Travel and Conferences	173,172	127,410
Client Transportation	100,387	120,923
Client and Other Wages	41,659	51,852
Client Support	102,922	105,889
State Provided Services	500,666	696,243
Capital Outlay (Under \$5,000)	94,850	55,513
Miscellaneous	43,606	11,054
Wraparound and Respite	21,493	23,159
	<u>\$6,031,552</u>	<u>\$6,185,698</u>
Total Operating Expenditures		

The notes to the financial statements are an integral part of this statement.



**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL
REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors
West Michigan Community Mental Health System
Ludington, Michigan

We have audited the financial statements of the West Michigan Community Mental Health System as of and for the year ended September 30, 2004, and have issued our report thereon dated November 17, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether West Michigan Community Mental Health System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered West Michigan Community Mental Health System's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management in a separate letter dated November 17, 2004.

This report is intended for the information of the audit committee, management, and the Board of Directors, and is not intended to be and should not be used by anyone other than these specified parties.


Roslund, Prestage & Company, P.C.
Certified Public Accountants

November 17, 2004



MANAGEMENT LETTER

Board of Directors
West Michigan Community Mental Health System
Ludington, Michigan

In planning and performing our audit of the financial statements for West Michigan Community Mental Health System for the fiscal year ended September 30, 2004, we considered the internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure.

However, during our audit we became aware of matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters.

This letter does not affect our audit report dated November 17, 2004 on the financial statements of West Michigan Community Mental Health System.

We will review the status of these comments during our next audit engagement. We have discussed these comments and suggestions with management, and will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Sincerely,



Roslund, Prestage & Company, P.C.
Certified Public Accountants

November 17, 2004

West Michigan Community Mental Health System
Management Letter

Perform a Fraud Risk Assessment

In light of the wave of notorious frauds involving large organizations in the last few years, such as Enron, WorldCom, and HealthSouth, there may be a misperception that fraud affects only large organizations. However, fraud occurs in organizations of all sizes, and almost any employee may be capable of perpetrating a fraudulent act given the right set of circumstances. In fact, fraud may be a more significant problem for small organizations. In the 2002 survey of its members conducted by the Association of Certified Fraud Examiners (ACFE), the median loss per fraud occurrence reported from businesses with 100 or fewer employees was \$127,500, a proportionately larger loss than the \$97,000 median loss in organizations with 10,000 or more employees.

Whereas the highly publicized frauds at large public organizations like Enron, WorldCom, and HealthSouth involved fraudulent financial reporting, for small organizations, one of the primary fraud risks is the ever-present risk of misappropriation of assets (theft), particularly fraudulent cash disbursements. The opportunity to commit and conceal fraud exists where there are assets susceptible to misappropriation and there are inadequate controls to prevent or detect the fraud. To address this risk, we recommend that West Michigan Community Mental Health System (the Authority) perform a risk assessment to identify, analyze, and manage the risk of asset misappropriation. Risk assessment, including fraud risk assessment, is one element of internal control. Thus, ideally, the Authority's internal control should include performance of this assessment, even though our annual financial statement audits include consideration of fraud.

The fraud risk assessment can be informal and performed by a management-level individual. Ordinarily, the management-level individual would conduct interviews or lead group discussions with personnel who have extensive knowledge of the Authority, its environment, and its processes. The fraud risk assessment process should consider the Authority's vulnerability to misappropriation of assets. When conducting the self-assessment, questions such as the following can be considered:

- Which individuals in the Authority have the opportunity to misappropriate assets? These are individuals who have access to assets susceptible to theft and to records that can be falsified or manipulated to conceal the theft.
- Are there any known pressures that would motivate individuals with the opportunity to misappropriate assets? Pressures may relate to financial stress or dissatisfaction. In assessing whether these pressures may exist, the assessor should consider whether there is any information that indicates potential financial stress or dissatisfaction of individuals with access to assets susceptible to misappropriation.
- What assets of the Authority are susceptible to misappropriation?

West Michigan Community Mental Health System
Management Letter

- Are there any known internal control weaknesses that would allow misappropriation of assets to occur and remain undetected?
- How could assets be stolen? Assets can be stolen in many ways besides merely removing them from the premises. For example, cash can be stolen by writing checks to fictitious individuals or vendors and cashing them for personal use. Inventory or other assets can be stolen through sales to fictitious customers. Assets can also be stolen by unauthorized trading in securities.
- How could potential misappropriation of assets be concealed? Because many frauds create accounting anomalies, the perpetrator must hide the fraud by running it through as an adjustment to another account. Generally, fraud perpetrators may use accounts that are not closely monitored.
- What factors might indicate that the Authority has a culture or environment that would enable management or individuals to rationalize committing fraud?

Once areas vulnerable to fraud have been identified, a review of the Authority's systems, procedures, and existing controls relating to the identified areas should be conducted. The Authority should consider what additional controls need to be implemented to reduce the risk of fraud. There are two basic types of controls—those that are designed to address specific types of fraud, and those that are more general in nature. General controls that reduce an individual's ability to commit fraud without detection include the following:

- Requiring Periodic Job Rotation and Mandatory Vacations. When an employee stays in the same position for a long period and has few absences, an opportunity exists for that employee to design and commit fraud schemes. Requiring key individuals to rotate jobs periodically or to transfer to different job functions is one way to address this fraud risk. Requiring all individuals to take an annual vacation, during which time others perform their job functions, also makes it more difficult for an employee who is committing fraud to continue concealing the fraud scheme.
- Preparing and Reviewing Monthly Financial Statements in a Timely Fashion. As previously mentioned, many frauds create accounting anomalies. Thus, one way to detect fraud on a timely basis is to review monthly financial statements and investigate unusual variances. If possible, these statements should include budget, prior period, and year-to-date amounts to help identify variances. Performing the review and investigation on a timely basis helps minimize the extent of potential fraud.

West Michigan Community Mental Health System
Management Letter

- Implementing an Employee Hotline. Tips and complaints from fellow employees or vendors have enabled many organizations to discover occurrences of fraud. Anonymous telephone hotlines allow honest employees and vendors who may fear retaliation from fraud perpetrators to report unethical behavior without risking exposure.

Examples of controls to prevent or detect specific types of fraud include the following:

- Independent Checks of work performed. Independent checks test another employee's work, such as by having a second employee re-perform or test an employee's work.
- Separation of Duties. Separation of duties is one of the most effective controls to prevent or detect misappropriations of assets. When possible, incompatible duties should be performed by different employees. For example, the responsibility for authorizing transactions, recording transactions, and maintaining custody of assets should be assigned to different people in the Authority to the extent possible.

When assessing the Company's internal control, the relationship between the nature and extent of fraud controls recommended and the cost of implementing those controls should be considered. For example, instead of trying to prevent fraud, the Authority may choose to use more detective controls to ensure that the fraud is identified and corrected in a timely fashion. Because detective controls are performed after the original transaction occurs, they may be easier to implement and more cost effective.

We would be pleased to provide more information about performing a risk assessment or assist management in performing one.